



## **Remarks by Mayor Jerry Sanders**

### **Announcement of City Remedial Plan**

**August 24, 2006**

Today, we formally deliver the City's responses to the 121 remedial recommendations made by Kroll.

For the past two weeks, our staff has literally worked around the clock, weekends included, to conduct the proper analysis, to ask the appropriate follow up questions, and to consult with experts in the field so that we could ensure that this report was as complete, as accurate and as thorough as possible. It has been a massive team effort that has involved all sectors of City government.

### **Implementation of Plan is "Once in a Generation Opportunity" for Reform**

I wanted to start today by setting context for the importance of these actions that I am announcing.

Today, I announce that I will enthusiastically accept all of the remedial recommendations made by Kroll. I believe that it's in the City's best interests to accept them and more importantly, to implement them.

There are two ways that we can choose to look upon the remedial actions. We can look upon them negatively as punishment being forced upon us or we can look upon them as a once-in-a-generation opportunity to establish a new set of best practices for ourselves and government bodies in similar situations.

For too long, San Diego has been held up as the example of how not to do things. We now have an opportunity to embrace reform and serve as an example of how a city can credibly get its affairs in order and move on to a very productive future.

In summary, we can be victims and obstructionists or we can be pioneers. I choose to be a pioneer.

Embracing the remedial actions will be the easy part. The hard part, which I intend to do wholeheartedly and beginning immediately, is to implement them all. I fervently believe that the time to act is now.

At the same time, I want to make sure that this issue is treated responsibly and that expectations are managed appropriately.

Our citizens have a right to understand what results will come from the adoption of this remedial plan and more importantly, what will not happen directly as a result of its adoption.

We have a long road ahead of us and there are no easy answers. The set of problems before us are complex and as such, the solutions will be similarly complex. The problems weren't created overnight and they can't be solved overnight either.

### **Implementation will Result in Transparency; Efficiency; Positive Signals to Market**

Let me tell you what the adoption of the remedial plan will result in. It will definitely result in far greater transparency in our financial reporting systems and practices; it will make City government more efficient and accountable to our citizens; and implementation of the plan will introduce sorely needed internal financial and managerial controls.

I believe that adoption of these actions will send positive messages to the bond rating agencies and the financial markets that we understand the depth of our past wrong doing **and** that we are prepared to institute corrective actions so that we never make the same mistakes.

All of these actions will give us the ability to once again access the public credit markets so that we can obtain much needed capital for public infrastructure projects.

### **Implementation will NOT solve City's Financial Problems**

What the implementation of this remedial plan will **not** solve is the City's financial problems. The implementation of this plan is merely one of many steps that it will take to solve these problems.

Only fundamental changes to the ways in which we budget – and more importantly, account for long term liabilities -- will solve the City's problems. I think that this is an important enough issue for our citizens to hear about that I intend to begin that conversation tomorrow.

The changes that I propose will involve sacrifice on the part of all parties – our citizens and dedicated city employees included.

### **Mayor has Given Careful Thought, Consideration to Recommendations**

For the past two weeks, my staff and I have given each of the 121 recommendations careful thought and consideration. We haven't just accepted them at face value. We have debated them and asked tough questions of each other. We believe that we have a good understanding of the impact of each.

But I also don't want to mislead anyone. While we have worked around the clock, we have also just had a little over two weeks to process the recommendations. As such, our plan of action will be, by definition, an ongoing process that will include refinement. Some of the changes, for

example, will require changes to our City Charter and/or Municipal Code. Other changes will involve the actions of City agencies such as the City's Retirement Board and the Centre City Development Corporation. There are many moving pieces.

We debated whether or not we should choose certain remedial actions over others. It would have been far too easy to rationalize our way out of some as too onerous or financially costly. In the end, I thought it was important enough to implement them all.

### **Recommendations are the “Right Thing to Do”/Reform is Necessary**

My thinking on this subject was influenced by three major elements.

First, I think that adopting and implementing these remedial recommendations is the right thing to do. By any standard measurement, **reform is necessary**.

The vast majority of the recommendations are logical and straightforward. They are nothing more than the institution of sound business practices. Many of them, in fact, have previously been made in reports by citizen groups that go back years.

So, what's the difference in between then and now? I think it's the responsibility of a strong mayor to bring the will to make changes. Some of the recommendations are appalling in how obvious they are; the changes should have made been instituted a long time ago.

The will, on my part, to make these changes now is the single most important difference. I hope and expect that voters will hold me and my fellow elected officials accountable as well for whether or not we implement these reforms.

Some would argue there has never been the money to effectively implement recommendations. There still isn't the money but we simply have no choice. And therefore, I will have some very hard choices to make. But again, I believe that the time to act is now.

Clearly, we need to proactively address and correct the clear and convincing patterns of mismanagement and negligence that Kroll clearly detailed.

The way to do that is by implementing processes that correct this behavior and being steadfast in our resolve that this will never happen again.

I am not persuaded by the argument that we should hold off on adopting a remedial plan until we hear from the SEC. I think most in this community would agree that we've waited long enough. The Kroll report painfully points out that delays have been the tradition, not the exception, at City Hall.

I do not believe that my actions will be inconsistent with what the SEC will want to see in the way of reform. In fact, it may very well be that the implementation of these reforms will not necessarily address all of the concerns of the SEC. I respect their judgment and will take appropriate action at that time.

We have no reason to believe that a final order from the SEC will stand in the way of accessing the public credit markets.

### **Auditors Want Remedial Plan Prior to Audits**

Secondly, KPMG and Macias Ginni & O'Connell, the City's outside auditors, have both told us that they are satisfied with the remedial steps found in the Kroll report. They have told us that if the City accepts and implements a comprehensive remedial plan that they will be prepared to issue audited financial statements. We need the outstanding audits for FY03, 04 and 05 to re-access the public credit markets.

Clearly, there were practical implications that weighed heavily on my consideration of the remedial actions. But I am also hopeful that it will spur a much needed cultural change at City Hall as well.

### **Financial Markets will Judge City on Remedial Actions**

Thirdly, and finally, I do believe that investors and the financial markets will judge us based upon if, how and when we implement our remediation plan. It's incumbent on us to put the proper remedial actions in place so that they can have confidence that what previously happened at City Hall never happens again.

### **Mayor Speaks to Three Remedial Actions**

While Jay Goldstone will brief you on all of the remedial actions in a few moments, I would like to speak briefly to three of the recommendations: the appointment of a monitor; the establishment of an Audit Committee; and the establishment and appointment of an Auditor General.

I wanted to share with you my thinking on these three issues. I favor each for an entirely different reason.

With respect to the monitor, it's my belief that the SEC will make it a requirement in their order. If you look at past SEC orders, they have almost always required a monitor for an extended period of time. So why not agree to it now?

With respect to the establishment of a permanent and independent Audit Committee, my thinking was as follows: going back a number of years, the Government Finance Officers' Association, recommended the establishment of audit committees as a best practice.

Let me be clear: my conception of the permanent Audit Committee is very different from Kroll's role as the Audit Committee. I believe that we will be able to find qualified professionals from our own community that will be able to serve on this committee without compensation.

Given the City's problems in the past, this is an area in which I believe that an additional set of independent eyes is a good thing.

And lastly, with respect to the establishment and appointment of an Auditor General, I have stated previously that in order to ensure good, solid financial controls – that the auditor functions and the comptroller functions should be separated.

I think we need to do everything possible to send a message of unqualified reform to the financial markets. And I believe that the level of independence that this individual will be granted will do just that.

I support these three recommendations just as Kroll has made them. As such, it is critical, in my estimation, that I have the power to appoint all the individuals to all three of these functions with the requisite Council confirmation.

### **Mayor Calls Himself “Ultimate Monitor”/Responsible for Implementation**

While all three of these new offices will be critical players in setting things right, I am telling voters today that as their strong mayor, I am ultimately the responsible party for implementing the remediations and getting this City back on track.

I will be the ultimate monitor that ensures our compliance. While I didn't create these problems, I am responsible for fixing them. It will be my legacy to leave behind a better City government than the one that I inherited.

### **Timeframes/Deadlines Require Full Cooperation of City Attorney and City Council**

Today, I will deliver to the City Council a 38 page plan of action that includes timeframes and projected cost estimates.

You will see that the timeframes are appropriately aggressive. I will recommend that all of the actions be implemented over the next 30 months. Our ability to fulfill the dates hinge on the cooperation of the City Attorney and the City Council to draft and consider the various changes that I am proposing.

I don't anticipate any problems but I will not hesitate to speak out if I think that anyone is holding up the implementation of any of these reform efforts. The public expects us to work as a team to fulfill their long-awaited expectations of reform.

I should also point out that there has been a temptation in the past for decision makers to buckle under to vested interests. I can tell you that I won't allow it to happen this time, at least where I am concerned, and I will not hesitate to speak out if I believe that it is occurring.

These remedial steps are bigger than any one vested interest. This is bigger than all of us – it's about the City's future.

### **Fundamental Financial Reform is Needed at All Levels**

Let me turn now to the City's financial picture to include the costs of the remedial plan. Again, I want to emphasize that the implementation of this plan will not address the City's chronic financial problems.

Without widespread, fundamental financial reform at all levels, those problems will never be corrected. In fact, without reforms, the City will not be able to afford the cost of the remedial plan.

I think that this plan gives me a very valuable opportunity to make important changes to the cost centers of City government.

### **City Cannot Afford Employee Benefits and City Services**

As I have said previously, I think the cost of the benefits that we provide to our employees combined with the costs of the services that we provide to our citizens is unsustainable.

It's simply not realistic to believe that we can continue to operate in this kind of chaotic budgetary environment. We end up doing nothing right.

### **Remedial Costs Estimated to be Upwards of \$45 million**

It's our early estimate that the implementation of the remedial actions will cost upwards of \$45 million over the next 7 years alone. This is a very conservative estimate that will be subject to refinement.

In addition, there are a number of other issues, separate from those that can clearly be defined as remedial actions, that the City would have – or should have -- had to pay anyway.

To date, there has not been a game plan on how to pay these obligations. I will put one forward.

These include such line items as: the cost ramifications of the manner in which the Retirement System addresses net gains and losses; the cost increase that could come from the Retirement System adopting a revised amortization schedule; tax compliance for the past retiree healthcare payment liabilities; increased payments to address our deferred maintenance; increased contributions to fund the UAAL for retiree healthcare; and increasing our capital reserves to reduce the cost of borrowing.

We have yet to determine the total magnitude of the issue. In the spirit of greater transparency and so that we can get a sense of the total costs associated with the remedial actions, I have asked our CFO to work toward grouping all of the costs together.

### **Mayor will Issue City's First Ever 5 Year Budget Plan**

I firmly believe that any conversation about the costs of the remediation plan should be held within the broader context of the City's long range financial picture. I did not think it would be responsible to piece meal this discussion.

As such, I intend to present the Council with the City's first-ever 5 year budget plan. The plan will include the costs of the remedial actions as well as the other line items I just detailed. It's my goal to present this plan to the Council by the end of the year.

The plan will provide a roadmap for how we get the City back on more stable financial footing.

### **Mayor does NOT Support Tax Increases**

I want to be clear that I will not propose or support any tax increases.

I think that voters appropriately expect that government should be able to live within its means, just as citizens do in their own homes across our City. Consequently, we will have to make cuts to the costs of operating City government.

This is one of the reasons why I place such importance in BPR, or business process re-engineering. The reviews that are going right now will help us to make government more efficient, to reduce costs by eliminating waste and by working to maximize revenues.

### **Mayor Envisions Tough Decisions on Horizon**

But ultimately, I believe that there will also be some tough decisions on the horizons.

I will communicate all of my budgetary proposals, including how we account for long term liabilities, as part of my 5 year plan. I don't want to go too far because we are still in the development stages for the budget plan but I think that it's safe to say that I envision a much smaller City workforce in the future.

I also believe that City services will have to match our resources and our priorities. We can't – and won't – be all things to all people. Our resources simply won't allow it.

I have often said that I can't print money. Even when we succeed in making government as efficient as it can possibly be, there will still be an important element of sacrifice needed to get this City back on track.

### **Mayor Presents Timeline for Accessing Financial Markets**

Lastly, tomorrow, we will also present a new timeline for re-accessing the public credit markets.

Jay Goldstone will review this at the end of his presentation today but it's my sense that right now that we should have ratings by the end of February of next year.

This would mean that by no later than the beginning of June of next year, the City should be able to begin long-delayed major infrastructure projects.

I will end by saying that this is a major step in moving the City forward toward greater managerial and financial stability.

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